

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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to: Wendy E. Speelman
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Fed-State and Local Government
(Tax Exempt and Government Entities)

from: Blaise Dusenberry
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subject: 1099 Requirement and Deposit Refunds/Garnishment

This memorandum responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUES

1. Whether an County Clerk of Court is required to issue a Form 1099 to an attorney when the Court sends a debtor's garnished funds to a creditor's attorney, or to an attorney where the attorney is the creditor.
2. Whether an County Clerk of Court is required to issue a Form 1099 to an attorney who is refunded their client's money at the end of a case.
3. Whether an County Clerk of Court is required to issue a Form 1099-S, *Proceeds From Real Estate Transactions*, on foreclosure real estate transactions.

CONCLUSIONS

1. An County Clerk of Court is not required to issue a Form 1099 to an attorney when the Court sends a debtor's garnished funds to a creditor's attorney.
2. An County Clerk of Court is not required to issue a Form 1099 to an attorney who is refunded their client's money at the end of a case.
3. An County Clerk of Court is not required to issue a Form 1099-S, Proceeds From Real Estate Transactions, on foreclosure real estate transactions.

BACKGROUND INFORMATION

In , justices of the Supreme Court, and the judges of the court of appeals and the court of common pleas are elected on a nonpartisan ballot.¹ There is a court of common pleas in each of the counties.² Specific courts of common pleas are divided into separate divisions by the General Assembly, including general, domestic relations, juvenile and probate divisions. County Clerks of Court are elected for year terms.³ The Clerk of Court's duties include filing, docketing, indexing and preserving all court pleadings for civil, felony criminal and domestic relations cases. The Clerk of Courts also accounts for all monies collected, and issues writs to carry out Court orders including summons, subpoenas, warrants to arrest and death warrants in capital cases. Payments made by the County Clerks of Court include garnishments and refunds of deposits. Your office has inquired whether Clerks of Court are required to file and furnish payee statements in particular circumstances. We have analyzed these situations under two potentially applicable reporting provisions. We stress that the analysis discussed here does not apply to any other factual scenario.

REPORTING REQUIREMENTS IN GENERAL

There are several potential reporting provisions that may apply to County Clerks in the course of their business. One applicable reporting requirement is that set forth in section 6041(a), which provides, in pertinent part, that all persons engaged in a trade or business and making payment of fixed or determinable gains, profits, or income in the course of that trade or business to another person of \$600 or more in a tax year must report those payments in information returns filed with the Internal Revenue Service, and furnish written statements to the recipients of the payments. Treas. Reg. § 1.6041-1(i) provides that payments made by a state or a political subdivision are subject to this reporting requirement. Under the separate definitions set forth in Treas. Reg. § 1.6041-1(e), sometimes referred to as the middleman regulations, a person that makes a

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² The Court of Common Pleas are established by the

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payment in the course of its trade or business on behalf of another person is the payor⁴ that must make the information return for that payment if the payment is one that must be reported under I.R.C. § 6041 and if, under all the facts and circumstances, that person:

1. Performs management or oversight functions, that is, performs more than mere administrative or ministerial functions, Treas. Reg. § 1.6041-1(e)(1)(i), or
2. Has a significant economic interest in the payment. Treas. Reg. § 1.6041-1(e)(1)(ii).⁵

A second applicable reporting requirement is provided by section 6045(f), which requires that all persons engaged in a trade or business who make certain payments to attorneys in connection with legal services in the course of that trade or business must report those payments in information returns filed with the Internal Revenue Service and furnish written statements to the recipients of the payments. The reporting requirement under Section 6045(f), however, does not apply to any payment which is required to be reported under Section 6041(a). See I.R.C. § 6045(f)(2)(B); Treas. Reg. § 1.6045-5(c)(4).

Treas. Reg. § 1.6045-5(d)(3) contains its own definition of the term “payor” and defines a payor for section 6045 purposes as a person who makes the payment if that person is:

1. an obligor on that payment, or
2. is the obligor’s insurer or guarantor, see Treas. Reg. § 1.6045-5(d)(3).

The regulation further defines a “payor” to include a person who pays a settlement amount to an attorney of a client who has asserted a tort, contract, violation of law, or worker’s compensation claim against the person, and the person’s insurer if the insurer pays the settlement.

⁴ The definition of “payor” under Treas. Reg. § 1.6045-5(d)(3) is different from the definition under Treas. Reg. § 1.6041-1(e).

⁵ If two or more meet the requirement for making the return of information under Treas. Reg. § 1.6041-1(e), the person obligated to make the payment is the person closest in the chain to the payee, unless the parties agree in writing that one of the other parties meeting the requirement in Treas. Reg. § 1.6041-1(e) will report the payment. Treas. Reg. § 1.6041-1(e)(2).

FACTS AND ANALYSIS

Issue 1. Whether an _____ County Clerk of Court is required to issue a Form 1099 to an attorney when the Court sends a debtor's garnished funds to a creditor, or to the creditor's attorney.

You describe a situation where a creditor files suit to collect a debt, and the Court orders the debtor's funds, usually wages, garnished to pay the debt. The Clerk of the Court collects the garnishment proceeds, and forwards them to the creditor. The Clerk is also authorized under _____ law to collect a "poundage fee" in garnishment actions. Similarly, a criminal defendant ordered to make restitution to the victim may make a remittance to the Clerk of the Court, who will forward the remittance to the victim.

Section 6041(a)

We first examine whether section 6041(a) applies to require reporting by _____ Clerks of Court of a payment of a debtor's garnished funds to a creditor. We agree that the amounts may constitute fixed or determinable gains, profits, or income to the creditor for purposes of section 6041(a). The analysis does not end there, however. In order for section 6041(a) reporting to apply, the Clerk must meet the separate definition of a "payor" for purposes of the reporting requirements under section 6041(a) and Treas. Reg. § 1.6041-1(e).

It is our view that since _____ County Clerks of Court neither perform management or oversight functions, nor have a significant economic interest in the payment, they do not meet the definition of "payors" that must make an information return when they send a debtor's garnished funds to a creditor's attorney or to an attorney where the attorney is the creditor under the middleman regulations pursuant to I.R.C. § 6041(a).

When a debtor's garnished funds are paid through an _____ County Clerk of Court to a creditor's attorney, or to an attorney where the attorney is the creditor, the source of the payment and the original "payor" is the debtor. Under the middleman regulations under Treas. Reg. § 1.6041-1(e), however, a person will be considered a payor if the person performs management or oversight functions, that is, performs more than mere administrative or ministerial functions, see Treas. Reg. § 1.6041-1(e)(1)(i), or has a significant economic interest in the payment, see Treas. Reg. § 1.6041-1(e)(1)(ii). The regulation states that an example of a person that would not be required to make an information return under these regulations is a person that merely writes checks at the direction of others in connection with a transaction, because that person is performing a task that is merely administrative or ministerial. See Treas. Reg. § 1.6041-1(e)(1).

The determination of whether a person performs management or oversight functions with respect to a payment made on behalf of another, or has a significant economic interest in connection with that payment, is a factual one. Examining the role of County Clerks of Court, we conclude that they do not perform management or oversight functions under Treas. Reg. § 1.6041-1(e)(1)(i). Although _____ County Clerks of Court

make garnishment payments, the true source of the payments is the debtor. The funds are distributed pursuant to Court orders.⁶ An County Clerk of Court has no discretion in making the payments.⁷ We conclude that County Clerks of Court do not perform management or oversight functions with respect to these payments as they are merely performing their administrative and ministerial duties.

We have also considered whether the Clerk of the Court has a significant economic interest, particularly in light of the “poundage fee” being collected. The determination of whether a person has a significant economic interest in connection with that payment is a factual one. Court clerks are authorized under statute to subtract a poundage fee in garnishment actions.⁸ Even though the “poundage fee” is paid over to the Clerk, we conclude that County Clerks of Court do not have a significant economic interest in the payment under Treas. Reg. § 1.6041-1(e)(1)(ii).

Treas. Reg. § 1.6041-1(e)(1)(ii) states that a significant economic interest in a payment is “an economic interest that would be compromised if the payment was not made, such as by a mechanics lien on property to which the payment relates, or a loss of collateral.” A poundage fee is not similar to a mechanics lien, which is a statutory interest that a creditor has in another’s property that secures payment for labor or materials supplied in improving, repairing, or maintaining real or personal property. Neither is a poundage fee similar to a loss of collateral. Collateral is property that is pledged as security against a debt, or property that is subject to a security interest. A poundage fee does not involve security or a security interest, rather, it is a percentage commission awarded for money recovered under a judicial process, such as an execution.

Examples under Treas. Reg. § 1.6041-1(e)(5) further illustrate the meaning of a significant economic interest in the context of retaining a commission and provides:

⁶ Whether a judge in the exercise of his judicial duties in collection actions is subject to information reporting responsibilities under the middleman regulations is a close call and this memorandum does not express an opinion on that issue. We note, however, that neither I.R.C. § 6041 nor Treas. Reg. § 1.6041-1(e) (the middleman regulations) expressly address court ordered payments. By analogy, we note that I.R.C. § 60501(g) addressing information reporting of cash receipts of over \$10,000 specifically subjects criminal court clerks to the filing requirements. If judicial entities were not already excluded from information reporting requirements, I.R.C. § 60501(g)’s provision subjecting criminal court clerks to the Form 8300 reporting requirement would not be necessary. In any event, the issue of who should report payments under the middleman regulations would be obviated if the court order of distribution or order to disburse garnished personal earnings provided that defendants were responsible for information reporting requirements under section 6041.

⁷ Treas. Reg. § 1.6041-1(e)(5) Examples 3 and 6.

⁸ A poundage fee is an amount allowed to the sheriff, for certain services specified by statute which the court or its clerk shall tax in the bill of costs against the judgment debtor or those legally liable for the judgment.

Example 6. Literary agent J receives a payment from publisher L of fees earned by J's client, author K. J deposits the payment into a bank account in J's name. From time to time and as directed by K, J makes payments from these funds to attorneys, managers, and other third parties for services rendered to K. After subtracting J's commission, J pays K the net amount. J does not order or direct the provision of services by the third parties to K, and J exercises no discretion in making the payments to the third parties or to K. J is not performing management or oversight functions and does not have a significant economic interest in the payments and is not subject to the information reporting requirements of section 6041 in connection with the payments to K or to the third parties. For the rules relating to L's obligation to report the payment of the fees to K, see paragraphs (a)(1)(i) and (f) of this section. For the rules relating to K's obligation to report the payment of the commission to J and the payments to the third parties for services, see paragraphs (a)(1)(i) and (d)(2) of this section.

Thus, under Example 6, retention of a commission by a literary agent does not constitute a significant economic interest. We believe that retention of a commission is analogous to retention of a poundage fee, and accordingly we conclude retention of a poundage fee in garnishment actions under the applicable statute by County Clerks of Court does not constitute a significant economic interest in the payment.

Since County Clerks of Court neither perform management or oversight functions, nor have a significant economic interest in the payment, they do not meet the definition of "payors" that must make an information return under the middleman regulations pursuant to I.R.C. § 6041(a). Since the middleman regulations do not apply,⁹ the general rule of section 6041 would apply to these facts. Under the general rule of I.R.C. § 6041, the filing and furnishing requirement falls upon the payor that is source of the payment. Here, assuming all the other criteria of section 6041 are met, that person is the debtor\garnishee.

Section 6045(f)

Since there is no reporting requirement under section 6041(a), we next turn to the applicability of section 6045(f), see I.R.C. 6045(f)(2)(B). We conclude that the provisions of section 6045(f) do not require an County Clerk of Court to issue a Form 1099 to an attorney when the Court sends a debtor's garnished funds to a creditor's attorney. We believe that in this situation, the Clerk of the Court does not meet the definition of a payor set forth in Treas. Reg. § 1.6045-5(d)(3). The Clerk is neither an obligor on the payment, nor the obligor's insurer or guarantor.

⁹ See footnote 7.

An obligor is colloquially defined as “One who has undertaken an obligation; a promisor or a debtor.” BLACK’S LAW DICTIONARY (7th ed. 1999). Webster’s Dictionary defines the term “obligor” as “one that binds himself or gives his bond to another [or] one that places himself under a legal obligation.” WEBSTER’S THIRD NEW INTERNATIONAL DICTIONARY 1556 (3d ed.1981); *Taylor Elec. Services, Inc. v. Armstrong Elec. Supply Co.*, 167 S.W.3d 522 (Tex.App. 2005)(citing WEBSTER’S). The comments to the Restatement (Second) of Contracts on Section 316 on assignments of rights and delegation of duties under a contract in its comments define an obligor as “[a] person subject to a duty.”¹⁰ These definitions do not describe a court clerk. Clerks receive filing fees and deposits pursuant to Court rules and court orders, and disburse funds upon request by court order. Performing this function does not make the Clerk of the Court a party to the debt. Receiving mandated fees and deposits does not convert a Clerk of Court into an obligor, or an obligor’s insurer or guarantor. We believe the same result is true of criminal restitution payments.

In conclusion, an _____ County Clerk of Court is not required to issue a Form 1099 to an attorney when the Court sends a debtor’s garnished funds to a creditor’s attorney, because the Clerk of the Court is not a payor for purposes of the reporting requirements under I.R.C. § 6045(f). We reach this conclusion because the County Clerk of Court is neither an obligor on the payment, nor the obligor’s insurer or guarantor under Treas. Reg. § 1.6045-5(d)(3). Further, County Clerk of Court is not a payor for purposes of I.R.C. § 6041 as it is only making payment on behalf of another and neither performs management or oversight functions, nor has a significant economic interest in the payment for purposes of the reporting requirement under I.R.C. § 6041(a) under Treas. Reg. § 1.6041-1(e)(1)(i) and (ii).

Issue 2. Whether an _____ County Clerk of Court is required to issue a Form 1099 to attorneys who are refunded their client’s money at the end of a case.

Although your request was not specific, you indicated that in some cases, a party to a civil action in an _____ court may deposit filing fees with the Clerk of the Court. At the close of the litigation, the Clerk will return the unused fee to the party’s attorney. You argue that the Clerk of Court is not required to issue a Form 1099 to an attorney whose client’s money has been refunded at the end of a case. We agree.

Section 6041(a)

We first examine whether section 6041(a) applies to require reporting by _____ Clerks of Court of a payment to attorneys when their client’s funds are refunded at the end of a case. It is our view that section 6041 does not impose a reporting requirement in this situation. Under section 6041(a), every person engaged in a trade or business must file an information return for payments made to another person in the course of the payor’s

¹⁰ RESTATEMENT (SECOND) OF CONTRACTS § 316 cmt. c (1981).

trade or business that constitutes fixed or determinable **income**. Payments that are not includible in the recipient's income need not be reported.

Treas. Reg. § 1.6041-1(c) of the regulations provides that income is "fixed" when it is paid in amounts definitely predetermined. Income is "determinable" when there is a basis of calculation by which the amount to be paid may be ascertained.

Under Treas. Reg. § 1.6041-1(a) and (c), a payor generally is not required to make a return under section 6041 for payments that are not includible in the recipient's income, nor is a payor required to make a return if the payor does not have a basis to determine the amount of a payment that is required to be included in the recipient's gross income. The Supreme Court has defined income as "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955). A deposit made and returned to a taxpayer generally does not constitute an accession to wealth.

I.R.C. § 111(a) provides that income recovered during the taxable year is excluded from gross income for that year as long as the amount of the recovery did not reduce prior Federal income taxes, that is, the taxpayer did not a deduction for the deposit amount.¹¹ Income is determinable when there is a basis for calculating the amount to be paid. Treas. Reg. § 1.6041-1(c). Where the payor cannot determine whether the payment is includible in the recipient's income, reporting is not required because the amount paid is not fixed or determinable income.¹² Here, the County Clerk of Court does not have the information whether the taxpayer who made the deposit took a deduction and received a tax benefit for the amount deposited. Accordingly, an County Clerk of Court is not required to issue a Form 1099 to attorneys who are refunded their client's money at the end of a case.

Section 6045(f)

Since there is no reporting requirement under section 6041(a), we next turn to the applicability of section 6045(f), see I.R.C. 6045(f)(2)(B). We conclude in this particular instance that the Clerk of Court is not required under I.R.C. § 6045(f) to issue a Form 1099 to attorneys who are refunded their client's funds because the Clerk of Court is not a payor for purposes of the reporting requirement under I.R.C. § 6045(f) because it is neither an obligor on the payment, nor the obligor's insurer or guarantor, under Treas. Reg. § 1.6045-5(d)(3).

As discussed above, I.R.C. § 6045(f) requires that all persons engaged in a trade or business who make certain payments to attorneys in connection with legal services in the course of that trade of business must report those payments in information returns filed with the Internal Revenue Service and furnish written statements to the recipients

¹¹ See also Treas. Reg. § 1.111-1.

¹² See Rev. Rul. 80-22, 1980-1 C.B. 286.

of those payments. Just as in Issue 1, an County Clerk of Court is not required under I.R.C. § 6045(f) to issue a Form 1099 to attorneys who are refunded their client's fee deposit at the end of a case, because the Clerk of Court is not a payor as defined in Treas. Reg. § 1.6045-5(d)(3). Under that regulation, the Clerk is neither an obligor on the payment, nor the obligor's insurer or guarantor. County Clerks of Court in the course of their trade or business are merely performing their administrative and ministerial duties and are thus not subject to the information reporting requirements of I.R.C. § 6045(f) where they are returning a fee deposit.

Issue 3. Whether an County Clerk of Court is required to issue of a Form 1099-S on foreclosure real estate transactions.

Finally, you inquired whether the Clerk of Court's involvement in a foreclosure action imposed a reporting obligation on the Clerk for the foreclosure amount. We agree that an County Clerk of Court is not required to issue Form 1099-S, *Proceeds From Real Estate Transactions*, on foreclosure real estate transactions. The acquisition of U.S. property by foreclosure must be reported **by the lender** who held the property as security for a loan to a non-exempt borrower on a Form 1099-A, *Acquisition or Abandonment of Secured Property*.

Although in general gross proceeds of \$600 or more from the sale or exchange of most real estate must be reported by a real estate reporting person¹³ under I.R.C. § 6045(e), no information return or information statement is required under this section for transfers in full or partial satisfaction of a debt secured by the property, including foreclosures, transfers in lieu of foreclosures, or abandonments, see Treas. Reg. § 1.6045-4(c)(1)(ii). Under I.R.C. § 6050J, any person who, in connection with his trade or business, lends money secured by property and who in full or partial satisfaction of any indebtedness acquires an interest in that property or has reason to know that the property has been abandoned, must file a return with the Internal Revenue Service¹⁴ and furnish a statement to the debtor.¹⁵ Accordingly, the reporting requirement under I.R.C. § 6050J is imposed only on lenders who make secured loans in connection with a trade or business.¹⁶

¹³ For purposes of the real estate reporting rules, a real estate reporting person is any of the following persons who are involved in a real estate transaction, in the following order:

- (1) The person (including any attorney or title company) responsible for closing the transaction, I.R.C. § 6045(e)(2)(A);
- (2) The mortgage lender, I.R.C. § 6045(e)(2)(B);
- (3) The transferor's broker, I.R.C. § 6045(e)(2)(C);
- (4) The transferee's broker, I.R.C. § 6045(e)(2)(D);
- (5) Any other person designated in regulations, I.R.C. § 6045(e)(2)(E).

¹⁴ I.R.C. § 6050J(a).

¹⁵ I.R.C. § 6050J(e).

¹⁶ Treas. Reg. § 1.605-J-1T Q-1, Q-15. Although under I.R.C. § 6045 (e), real estate transactions are generally reported on a Form 1099-S, *Proceeds From Real Estate Transactions*, brokers are exempt from

Reporting of foreclosures by lenders under I.R.C. § 6050J is made on a Form 1099-A.¹⁷ If a lender cancels a debt of more than \$600 in connection with a foreclosure or abandonment of secured property, the lender need not file both Form 1099-A and Form 1099-C, *Cancellation of Debt*, for the same debtor, and may file Form 1099-C only.¹⁸

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the reporting requirement under I.R.C. § 6045(e) in the case of foreclosures, see Treas. Reg. § 1.6045-4(c)(1)(ii).

¹⁷ 2015 Instructions for Forms 1099-A and 1099-C, Acquisition or Abandonment of Secured Property and Cancellation of Debt, at 1.

¹⁸ *Id.* at 3.